

Rights of Minority Shareholders

Commission in charge of the Session:

International Business Law Commission (IBLC)

London, 2015

National Report of Iran

Encyeh Seyed Sadr

Bayan Emrooz Law Firm
Shahrokh Alley, Africa Blvd. (Jordan)
1915713383, Tehran, Iran
+9821 2620 3634
Encyeh.sadr@bayanemrooz.com

General Reporter

Ricardo Chacon, Chacon & Rodriguez S.C
Mexico City, Mexico
rchacon@chro.com.mx

12 May 2015

INTRODUCTION

A shareholder without voting strength or power to influence decision making on his own it's considered a minority shareholder. To be a minority shareholder could be tricky when it comes to protect your investment and its fruits. To avoid abuses from the majority, rules to protect minorities have been put in place in many jurisdictions. As for example, shareholder's agreements, the right of minorities to appoint a Director or other officers, rights to sell or buy shares at a fair value, the right to convene general assembly's, the right to get information from the management, etc.

Somehow, these rights may get in conflict with a fast decision making capability, impairing the management or the majority shareholders, which in turn may be a form of abuse from the minorities.

Therefore we would like to find out how these minority rights are handled in different jurisdictions.

Questionnaire on rights of *minority shareholders*

1. Current scenario at your jurisdiction:

1.1. How and to what extent are *minority shareholders* protected in publicly and privately held corporations in your country, either as to legal or firm level protection?

(The main legal source with respect to the rights of the minor shareholders in Iran is the Commercial Code of Iran (CCI) ratified in 1933 that covers the general regulations with regard to different types of companies, shareholders, board meetings, managers and inspectors. Few articles in the CCI are considered as the protective regulations with regard to the rights of minority shareholders in both public and private joint stock companies.¹

Recently Tehran Stock Exchange ratified an instruction called the By-Law on the Principles of Corporate Governance that provides guidelines on the corporate governance in public stock companies, principles of which could be voluntarily be taken by the directors and managers in both public and private joint stock companies.

Besides the above Act and Instruction, the Law on Using Services of Professional Accountants has been ratified in 1994 (its by-law ratified in 2008). Nevertheless, Iran regulations suffer from having no specific law and regulation that would duly and directly address the issues of corporate governance.

The four preliminary principles of Corporate Governance i.e. fairness, transparency, accountability and responsibility have not been referred in Iran's regulations; though some instructions are available with this respect in the Principles of Corporate Governance ratified by the Tehran Stock Exchange.)

¹ Article 88 (collective voting right for appointment of the directors), Article 139 (right of shareholders to be informed of the financial status, annual bill and transactions of the company before holding the general meeting), Article 95 (possibility for the shareholders to claim against directors).

1.2. Do they have in essence real choices, or are the ones that are in the hands of the dominant group, either managers or major shareholders, or are they restricted to those that do not challenge the majority power, representing the status quo?

(The minority shareholders have no much choice for effecting their will and opinion in the company. Although the general meetings (both ordinary and extraordinary) are arranged as a mechanism for presentation and voting of the shareholders, the quorum that has been predicted in the Commercial Code of Iran (CCI) at both levels i.e. holding the session and making decision, is dominated by the majority power. Accordingly for taking decision on the issues that contain benefits for the minority shareholders, such as distribution of the annual benefits or increase of capital with the right of share option, still the votes of majority of shareholders is needed to reach the nominated quorum in the CCI.)

1.3. Has the law and precedents of your country evolved in ways that increase *minority shareholders* ability to defend against expropriation by those in control (misuse of assets, reallocation of profits, transfer pricing, etc.) ?

(Generally speaking under the Commercial Code of Iran no specific procedure has been predicted for internal control of the power of major shareholders, although the inspectors who are appointed by the shareholders could play a crucial rule for observing the act of managers and transactions of the company. However in many cases appointment of the inspectors are conducted in a conventional behavior and as a formality. According to Article 8 (18) of the CCI the procedure for nomination of the inspectors and their number could be verified in the Articles of Association of the company.

At next stage the shareholders may have the rights to claim before the courts. Making claim at this stage on behalf of the company is also much harder than the personal claim of the shareholders as independent individuals.)

1.4. Is the legal dimension the prevalent one in the Corporate Governance (CG) atmosphere, or is the firm level CG the common manner to protect minorities?

(The legal dimension under the CCI set out the main rules with respect to the rights of shareholders including the fact that each share in the joint stock companies brings one voting right for the shareholder. Further the quorum for making decision in the general meetings of company has also been determined by the CCI. Accordingly not few options are remained to be agreed upon by the shareholders at firm level. Obviously in the Articles of Association (AoA) of a company agreement could be made on particular issues, but the nominated quorum in the CCI is an imperative rule that shareholders cannot agree otherwise.

Having Shareholder Agreement (SHA) is not also a common procedure in corporate law of Iran for guarding rights of minor shareholders. Nevertheless through collective voting, the minor shareholders could put all their voting shares together to be granted to one person, accordingly it could be likely for the minor shareholders to nominate a representative in the Board; although at Board level, still they lack the majority for taking decision based on the quorum of the Board.)

1.5. What is the role of ownership concentration in the protection of the minority?

(Depending on the type of companies, the ownership concentration differs. The joint stock companies (both private and public) that have the main economic role in the business activity of the country are considered ownership concentrated companies. According to Article 75 of CCI each share in the joint stock companies has one voting right. The main emphasis on this type of companies is on the capital, so basically the regulations are drafted in light of protection of holders of higher investment.

In the other types of companies that are based on the personality of the founders and shareholders, the voting rights may differ based on the liability of the shareholders. However since these types of companies have rarely fundamental role in Iran's economy, the answers for this report are provided based on the joint stock companies.)

1.6. Is benchmarking used as a mechanism for minorities to select the country or firm better suited to risk profile and protection from rights deprivation?

(Benchmarking process is not generally used in the private joint stock companies while operation of the public joint stock companies that are offered to public are assessed by market control.

The By-Law on the Principles of Corporate Governance prepared by the Stock Exchange of Tehran (2007) provides instruction on benchmarking and stipulates this rule as a tool for controlling the major power in the public joint stock companies. Though, it is not clear how much benchmarking actually effects on the operation of the managers and if the managers will consider that as a tool for observation in their companies.)

- 1.7. Is the formation of group dynamics among dispersed shareholders working in your country?

(According to Article 88 of the CCI, the procedure for appointing managers have been determined which is also one of mandatory rules of CCI. According to this Article the minor shareholders could collect their voting rights and dedicate it to one nominee, so that the named nominee would have greater chance to enter the Board. Although in the Board, the manager(s) nominated by the minority may still be under dominance of the majority power.)

- 1.8. What is the role of market liquidity in the *minority shareholders* exit option?

(It depends on the scope of business that the company is involved. In some sectors such as banking, the market is a liquid instrument and entrance and exit of the shareholders are easily conducted while in some other sectors, the market is illiquid. Also as most of the huge construction companies are owned and controlled by the public sector, the risk of illiquidity in those projects get higher subject to non-transparency.)

- 1.9. Have legal reforms in your country given tools to majority to use compliance as an instrument to somehow “legalize” minority expropriation?

(In the major private joint stock companies and public joint stock companies codes of conduct are using to discipline the internal governance, monitoring and creating compliance between different stakeholders. Relying on the code of conducts has also been instructed in the By-Law on the Principles of Corporate Governance of the Stock Exchange of Tehran. Nevertheless through making compliance and internal

formalities, the minority would not be expropriated as the major rules with respect to voting and required quorum are mandatory and are determined by the law while internal agreement could not make a change. However the main problem appears when the minor shareholders are kept at that level so that their votes would not make any change or effect on the decision-making process.)

2. Looking forward at your jurisdiction:

- 2.1. What is the way to avoid *minority shareholders* from suffering mayor shocks, -if applicable in your country- due to restrictive visions as to minority rights, without falling into abuses of minority rights? Is it possible to harmonize both?

(Since the economy of Iran is a public one and the major corporations in mother industries such as oil and gas, telecommunication, agriculture, mines and etc. are governmental and public, such scenarios happen rarely as either the giant governmental companies have no public shares or subject to granting shares to public it would be so minor with no right for decision making or influencing on the policies of the company. In other words the minority shareholders have to comply with the changes and shocks may happen to the company. There is no regulations in this respect to protect the rights of shareholders and the market control has also no fundamental role as the market per se is not competitive subject to dominance of the governmental companies.)

- 2.2. Is *minority shareholders* activism taking place in your country, and to what extent?

(Minority shareholders activism to some extent depends on the internal culture of each company. From legal point of view there are not many options available for the protection of the rights of minority shareholder. Normally the minor shareholders do not have the chance to influence on the policies and practice of the firm.

The role of minority shareholders could be found either in the general meetings, or through appointing a trustable inspector; through whom the managers would be put under questions for their decisions, transactions and performance in the company.)

- 2.3. What is the trend in your country for the protection of *minority shareholders*?

(The most popular trend for protection of minority shareholders is appointment of independent inspector(s). According to the By-Law on the Principles of Corporate

Governance of the Stock Exchange of Tehran, the public companies should appoint their inspectors from registered inspector institutions; however this obligation is not applicable with respect to private joint stock companies and appointment of the inspectors in this category of companies is conducted as a formality.

Otherwise there is no specific trend for protection of the rights of minority shareholders inside the companies' framework and referral before public courts could be considered as the general and final solution. Although even for this scenario it is not easy to make claims on behalf of company.)

- 2.4. What is the impact of the Sarbanes-Oxley Act (SOX) in your country, as a canon to regulate domestic capital markets and CG?

(The SOX did not directly affect on the laws of Iran. Iran for so many years has been considered as an isolated country with a traditional legal system. We also do not witness regular and fluent change of laws and regulations in the state's Parliament. There have been few modern regulations in respect of IT, E-Commerce, IP and arbitration, however issues related to corporate governance are still unfamiliar to the Iran's regulations. The ranking of Iran by the World Bank Doing Business in 2015 demonstrates lack of work and regulations in this respect².

Nevertheless, the law on Using Services of Professional Accountants (USPA) was ratified in 1994 and its By Law was ratified in 2008. The By-Law on the Principles of Corporate Governance of the Tehran Stock Exchange has also been ratified in September 2008 and the new Commercial Code of Iran has also been ratified by the Parliament but it is more than a year that this Code is pending for approval of the Guardian Council in order to become applicable.)

3. Precedent cases at your jurisdiction:

- 3.1. Please report some recent judicial cases regarding *minority shareholders* issues.

(As mentioned above, the Iranian economic system is a governmental one and as a result the major and big companies are owned and controlled by the government in the

² <http://www.doingbusiness.org/data/exploreeconomies/iran/>

forms of governmental or semi governmental companies. In case of occur of corruption or misuse of rights of minority shareholders, subject to lack of transparency, release of information would be limited.

Recently it has been reported that some big companies that were engaged with construction projects and refineries, defaulted in their financial records. The named companies had also offered shares to public while the value of shares at the stock exchange rated higher than the actual value. Claims now are pending against the companies and some demonstrations have been made by public shareholders before the stock exchange.³

With regard to private joint stock companies, subject to the size of companies that are normally small or medium, disputes and claims are also minor and raised among the controlling shareholders and managers without major effect on the public.)

³ Worldwide Broadcasting and Media.